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FM AMEMBASSY PARIS
TO RUEHC/SECSTATE WASHDC 3270
INFO RUEATRS/DEPARTMENT OF TREASURY WASHDC
RUCPDOG/DEPT OF COMMERCE WASHDC
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UNCLAS SECTION 01 OF 03 PARIS 001078

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SUBJECT: AIRBUS: FEARS OF DEFENSE TRADE CONTROLS HURT U.S. EXPORTS

REF: PARIS 850

This is the second of two cables on Airbus and U.S. interests. It was drafted by APP Toulouse with support from Paris and represents the Consul's farewell report at the conclusion of a three-year assignment. A previous message focused on Airbus' structure and reform.

¶1. (SBU) SUMMARY: In spite of significant efforts to accelerate processing of export control licenses at the State Department, U.S. and European aerospace companies continue to be sharply critical of the USG export control system. Their perception affects a major American export industry -- U.S. aviation exports (excluding Boeing airplanes) reached USD 42.6 billion in 2007. Competitive in terms of quality and price, U.S. companies assert that they are informally excluded from contract discussions due to fears about U.S. export controls. The standard view in Toulouse is that the U.S. export control licensing process is time-consuming, bureaucratic, unpredictable, and opaque rather than a tool for preventing proliferation and safeguarding national interests. This perception damages American firms and the U.S. balance of payments. A more aggressive outreach and transparency program could help change perceptions. END SUMMARY.

¶2. (SBU) Several high profile cases in recent years have increased fears and created the perception among European corporations that U.S. export controls are costly, complex, and unpredictable. In March 2006, the USG fined Boeing USD 15 million, L-3 Communications USD 2 million, and Goodrich USD 1.25 million, in connection with the sale of civilian aircraft to China that included a gyro microchip (QRS-11). In 2004, Northrop Grumman's use of an inertial sensor in a navigation system disrupted aircraft production at Airbus during three weeks while the USG determined whether the item required a license from State or Commerce. Assembly of eight A320 and A340 aircraft was halted (i.e. thirty percent of the assembly line) until Airbus replaced the twenty-four Northrop Grumman sensors with a Honeywell product. Had the delay lasted longer, or had it also affected Honeywell, which at the time was the only other supplier for this product, it could have completely stopped production at Airbus. Airbus officials and suppliers continue to recall vividly this experience. They emerged from it convinced that U.S. export controls were characterized by unclear jurisdictions and unpredictable and potentially costly administrative processes.

¶3. (SBU) More recently, the case of the flight safety qualification of Northrop Grumman's new inertial sensor has reinforced this view. The European Aviation Safety Agency (EASA) is conducting certification of the sensor, which contains International Traffic in Arms Regulations (ITAR)-controlled data. Northrop Grumman's interpretation of its Commerce license precludes it from sharing such information with EASA without a Technical Assistance Agreement (TAA), or signature of a bilateral safety agreement between the FAA and EASA that would resolve the issue since it specifically addresses the question of disclosing ITAR-controlled data for

certification purposes. Signature of the agreement has been repeatedly held up since June 2007 due to unrelated issues.

14. (SBU) U.S. suppliers frequently assert that their European competitors willingly play on European manufacturers' belief that the U.S. export control system is complicated and arbitrary in order to win contracts. They cite Airbus' recent decision to award Thales a sole source contract for the inertial system on its latest aircraft -- the A350. According to sources from two firms knowledgeable about A350 contract negotiations, Airbus rejected more technologically advanced options from American firms due to fear the USG would decide the item should fall under ITAR. The loss of this particular contract amounts to approximately USD 480 million over the life of the A350 program. U.S. companies worry however that they eventually will lose the entire Airbus market, estimated at USD 160 million per year, if Thales develops a competitive product not subject to ITAR controls.

15. (SBU) The inertial sensor issue first caused disruptions at Airbus as the company geared up for its first military product -- the A400M. Even though Airbus sought to use as many commercial components as possible to minimize the export control burden, this military program included a significant number of ITAR-controlled items and necessitated Airbus' first global approach to U.S. export controls. To address these issues, Airbus hired an Amcit as Vice President in charge of export controls. It then adopted a model TAA for use throughout the company and sought regular consultations with the State Department on pending applications. By all accounts, Airbus' applications for export licenses are now more consistent and better prepared. High-level sources at several companies involved with controlled items have noted the improved atmosphere, and in particular the positive impact of periodic Airbus-organized meetings in Washington between aerospace companies working on A400M export controls.

16. (SBU) In spite of this progress, several U.S. suppliers close to Airbus have told the Consul they believe Airbus will avoid American products on future military programs -- the A330 tanker excluded -- due to the company's belief that addressing U.S. export controls on the A400M has been too long, costly and complicated. Airbus and its suppliers complain that licenses take months to process, and that each modification of the original request requires additional delays. They trade horror stories such as that recounted by one representative of a large American aeronautic systems company, who recently told the Consul his firm has not received an answer to TAA amendments requested in July 2007.

17. (SBU) In the recently announced KC-45 contract, Airbus has structured production to minimize the impact of the licensing process, serving as prime subcontractor under Northrup Grumman. American business contacts have indicated that Northrop Grumman and EADS North America have agreed to perform as much work as possible in the U.S. with American citizens. Northrop Grumman will be solely responsible for the aircraft's militarization. Other European manufacturers with significant military business, such as Dassault and Eurocopter, also have long avoided American products for both their military and commercial programs. According to several American aeronautic system suppliers, in those cases in which the European business selected an American item for a commercial program, they carefully consider the consequences of using the same part number for a military product. They say that the companies fear that its application on a military program will "contaminate" it, rendering it ITAR-controlled and disrupting commercial production.

18. (SBU) In recent conversations, some American suppliers have argued that only fundamental reform of the export licensing process will change these attitudes. They advocate improving transparency, consistency, and response times through a program-wide license. Under such an approach, all exports of aviation parts for a given project would be covered by a single license. Instead of each American company applying for individual approval, the final manufacturer would ask for and obtain an overall license which would set the terms for all suppliers on the project. Whether or not this is a realistic proposition, the call for wide-ranging reform shows how negative attitudes toward U.S. export controls among large manufacturers have spread throughout the aerospace supply chain, even among American suppliers who are more familiar with the U.S.

system than their European competitors.

¶9. (SBU) Discussions between the Consul and procurement officials in Toulouse over the past three years suggest the problem is especially acute in small and medium-sized enterprises (SMEs). Because some procurement officials believe ITAR applies to all U.S. aviation products, they are reluctant to purchase anything "Made in the USA." Having heard the "horror stories" and with limited exposure to the actual U.S. system, they find it easiest to simply avoid American alternatives. In one-on-one meetings held as part of an outreach program last year, several European SMEs expressed their unfounded concern that they would be subject to ITAR should they purchase in the U.S. Since aircraft manufacturers increasingly are becoming integrators, subcontracting large sections of new airplanes (reftel), SME comprehension of the system is of growing importance and merits additional attention on the part of the USG.

¶10. (SBU) COMMENT: Over the course of the past year, the Department has made tremendous strides in response times, the area of greatest frustration to the aviation industry. Contacts have indicated that most TAAs and licenses now are returned within several months instead of the previous waiting time of six months. The Department's website indicates the average processing time is now 15 days compared to 35 days in March 2007. Because American suppliers have said any delay on a TAA can threaten a contract negotiation, they have strongly urged that State work to maintain this momentum, which is helping to reduce frustration among both American suppliers and European customers. More comprehensive reform, such as that advocated by some U.S. suppliers, is a proposition of a different order. While certainly meriting serious consideration, it would require a thorough policy review and substantial interagency consultation.

¶11. (SBU) Despite the improvements, too many European-based aviation representatives continue to see USG's export control licensing process as a "black hole" in need of fundamental reform. Many procurement officials in European companies also believe the USG eventually will use export controls as an economic weapon. These misunderstandings could be addressed by increasing USG export control outreach in Europe and continuing to engage recipients of American aviation technology regardless of nationality. Small and medium-sized companies will never have the resources to engage staff dedicated exclusively to this issue, but the USG could support U.S. exports by demystifying the system whenever possible. Over the past three years, the American Presence Post in Toulouse has organized highly successful seminars on Defense Trade Controls in Toulouse and at the Paris Air Show, as well as assisting with the planning of an event at this year's Farnborough Air Show in the UK. Regular Department participation in such conferences would greatly enhance their value, spread the good news about recent improvements in processing times, and help dispel some of the myths about trade controls that are costly to U.S. business and damaging to our legitimate interests in controlling the export of sensitive technology.

Stapleton